SCS Agency
Franchise Tax Board

SUMMARY ANALYSIS OF AMENDED BILL

Author: McPherson | Analyst: Roger Lackey | Bill Number: SB 83

Related Bills: See Legislative History | Telephone: 845-3627 | Amended Date: 02-25-97

Attorney: Doug Bramhall | Sponsor: ____

SUBJECT: PIT Rates/Deletes Lowest Bracket and Revises Remaining

____ DEPARTMENT AMENDMENTS ACCEPTED. Amendments reflect suggestions of previous analysis of bill as introduced/amended ________.

____ AMENDMENTS IMPACT REVENUE. A new revenue estimate is provided.

____ AMENDMENTS DID NOT RESOLVE THE DEPARTMENT'S CONCERNS stated in the previous analysis of bill as introduced/amended ________.

____ FURTHER AMENDMENTS NECESSARY.

____ DEPARTMENT POSITION CHANGED TO ________________________________.

____ REMAINDER OF PREVIOUS ANALYSIS OF BILL AS INTRODUCED/AMENDED ____________ STILL APPLIES.

__X__ OTHER - See comments below.

SUMMARY OF BILL

This bill would eliminate the 1% tax rate bracket for personal income taxpayers and revise the income threshold amounts for the remaining tax brackets.

SUMMARY OF AMENDMENT

The February 25, 1997, amendments eliminated all language regarding an earned income credit and added the new language discussed in this analysis.

EFFECTIVE DATE

This bill would apply to taxable years beginning on or after January 1, 1997.

SPECIFIC FINDINGS

Existing state law establishes six tax brackets, which determine the rate at which an individual's income is taxed. The tax rates range from 1% to 9.3% and are organized into tax rate schedules which chart the taxable income threshold amounts applicable to each tax rate. The progressive tax structure results in only a portion of the taxable income being subject to each rate bracket. Only that portion of taxable income exceeding the income threshold amount associated with the 9.3% rate is actually taxed at 9.3%. Thus, the average rate paid by all taxpayers is approximately 4%.

DEPARTMENTS THAT MAY BE AFFECTED:

____ STATE MANDATE ____ GOVERNOR'S APPOINTMENT

Department Director Position:	Agency Secretary Position:	**GOVERNOR'S OFFICE USE**
____ S ____ O	____ S ____ O	
____ SA ____ OUA	____ SA ____ OUA	Position Approved ____
__X_ N ____ NP	____ N ____ NP	Position Disapproved ____
____ NA ____ NAR	____ NA ____ NAR	Position Noted ____
________ PENDING	DEFER TO __________	
Department/Legislative Director Date	Agency Secretary Date	By: Date:
Gerald H. Goldberg 3/25/97		

An individual's taxable income passes to the higher marginal tax rate as their income increases. The result is a tax rate where that portion of income falling between each tax rate bracket is taxed at that specific rate until the taxable income exceeds the threshold amount of that rate until reaching the maximum 9.3% tax rate threshold. Only that portion of taxable income exceeding the 9.3% threshold is taxed at that rate.

Existing state law also provides a personal income alternative minimum tax (AMT) rate of 7%. The AMT was established to ensure that no taxpayers with substantial economic income avoid any tax liability by using exclusions, deductions, and credits (tax preference items). In calculating AMT, a personal exemption deduction is subtracted from the alternative minimum taxable income (AMTI) in the following amounts: $40,000 for married taxpayers filing joint returns; $30,000 for individuals filing as either single or as a head of household; and $20,000 for married taxpayers filing separate returns. This exemption deduction is intended to preclude the application of complex AMT rules to taxpayers with few tax preference items.

Existing state law requires the Franchise Tax Board (FTB) to index the tax brackets, the personal exemption credits, and the standard deduction each year based on the inflation rate.

This bill would eliminate the lowest PIT rate bracket of 1% for all PIT taxpayers, including head of household filers.

Also**, this bill** would decrease the taxable income threshold for the 2% bracket and revise the taxable income threshold of all remaining PIT tax rate brackets and therefore, each bracket's calculation of tax.

The revised taxable income threshold amounts in **this bill** represent the current bracket amounts for the taxable year beginning on January 1, 1987, and recomputed each year thereafter.

This bill also would make minor technical changes to the existing statute.

Policy Consideration

This bill lists the revised income tax brackets for the taxable year beginning on January 1, 1987. Current law provides that tax brackets listed in current law shall be recomputed for each taxable year beginning on or after January 1, 1988. It is the departments understanding that the author intended that the revised income tax brackets would be for the taxable year beginning on January 1, 1997. Amendment 1 is provided to allow the revised tax brackets would apply to the taxable year beginning on January 1, 1997, and that the income tax brackets would be recomputed each year for taxable years beginning on or after January 1, 1998.

The author's staff has indicated that the bill was intended to eliminate only the 1% tax bracket. This bill would go beyond that by also revising the remaining brackets resulting in a tax decrease for all income levels.

This bill would provide a tax benefit to low income taxpayers, but would provide a decreasing benefit as taxable income increases.

Implementation Considerations

Implementing this bill would require some changes to existing tax forms and instructions and information systems, which could be accomplished during normal annual update.

FISCAL IMPACT

Departmental Costs

This bill would not significantly impact the department's costs.

Tax Revenue Estimate

THE FOLLOWING TAX REVENUE ESTIMATE AND ANALYSIS REFLECT THE NEW RATES IN EFFECT BEGINNING JANUARY 1, 1997, AND ASSUMES INDEXING THEREAFTER.

It is understood that this was the author's intent.

Revenue losses are estimated to be:

Estimated Revenue Impact for SB 83 As Amended February 24, 1997 Effective after December 31, 1996 Assumed Enactment After June 30, 1997 Revenue Impact by Taxable Years ($in millions)		
1997	1998	1999
($92)	($93)	($94)

Revenue Impact by Fiscal Years ($in millions)		
1997-8	1998-9	1999-0
($129)	($93)	($94)

This analysis does not consider the possible changes in employment, personal income, or gross state product that could result from this measure.

Tax Revenue Discussion

Revenue losses under the Personal Income Tax Law would depend on the number of taxpayers who would have their tax reduced or eliminated by the removal of the 1% tax rate bracket and the revenue from the reduced 2% bracket.

The above estimates are based on the department's personal income tax model. These estimates do not reflect any behavioral impact that might occur as a result of these tax rate changes.

The following table reflects the tax changes by adjusted gross income classes:

Estimated Revenue Impact for SB 83 As Amended February 24,1997
Repeal 1% Tax Rate & Lower 2% Tax Bracket 1/
1997 Taxable Year
Returns & Tax Liability Changes
By Adjusted Gross Income Classes

Adjusted Gross Income Class	Returns 2/ With Changes	Percent of Total Returns With Changes	Total Tax Change	Average Tax Change	Tax Change As % of Total Tax Liability
	(thousands)		(millions)		
$0 to $20,000	1,768	19%	($14)	($8)	-7.8%
$20,000 to $30,000	1,593	17%	($14)	($9)	-2.6%
$30,000 to $40,000	1,368	15%	($14)	($10)	-1.5%
$40,000 to $50,000	1,072	12%	($11)	($10)	-1.0%
$50,000 to 100,000	2,593	28%	($29)	($11)	-0.5%
$100,000 to $150,000	513	6%	($6)	($12)	-0.5%
$150,000 and over	349	4%	($4)	($11)	-0.1%
Totals	9,256	100%	($92)	($10)	

1/ The above table reflects the tax changes by adjusted gross income as a result of repealing the 1% tax rate and reducing the starting point of the 2% rate bracket. The new brackets for this bill, starting with the 1997 tax year, are projected to begin at $2,850 for single and married filing separate filers and $5,700 for married filing joint, surviving spouse, and head of household. Under current law the two percent brackets are projected to start at $5,072/$10,145, respectively.

2/ Number of returns made non-taxable 400,000
Number of taxpayers made nontaxable, counting joint returns as two taxpayers 500,000

POSITION

Neutral.

The staff’s position is determined by administrative considerations and does not take into account tax policy considerations or revenue impact on the state. However, these issues are discussed in the analysis.

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FRANCHISE TAX BOARD'S
PROPOSED AMENDMENTS TO SB 83
As Amended February 25, 1997

AMENDMENT 1

On page 5, line 28, strikeout "1988" insert:

1998